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35-38 PORTMAN SQUARE

LONDON W1A 1HQ

FROM: Sir Michael Edwardes

8th March 1982

The Rt.Hon. Patrick Jenkin, MP,
Secretary of State for Industry,
Ashdown House,
123 Victoria Street,
London SW1.

CONFIDENTIAL

Dear Patrick,

FUTURE ORGANISATION OF BL

I am grateful to you for finding the time for an early meeting about the consultants' report, and I appreciate in particular your agreement to my request for Leslie Dighton to be present tomorrow. I have a number of important questions to raise with the consultants, and as their report is now in your possession I believe it is vital that you should hear those concerns - and the consultants' response - at first hand.

By way of preparation for tomorrow's meeting, I enclose our analysis of the consultants' report. It reflects the Board's first reaction to the report, though some of the concerns I shall voice tomorrow go beyond the scope of staff analysis. The paper stops short of an exhaustive point-by-point refutation, in the hope that it will be read by all those in Government who read the report itself.

M. Edwardes

** And of course
to ensure that the
Alpha will be
present. U*

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REPORT ON THE FUTURE ORGANISATION STRUCTURE OF BLBL's COMMENTS

1. The report's rejection of the BL Board's proposal for a split into two separate companies and its advocacy of a unified BL appear to rest on:-
 - a. a series of second-guesses of the Board's judgements about the future management of the company, particularly as regards the requirements for future leadership; and
 - b. two unsound and unsubstantiated assumptions relating to the privatisation of Land Rover.

LEADERSHIP

2. The consultants query the Board's judgement about the required "leadership configuration" for the next phase of BL's recovery. The consultants do not appear to contest the Board's view that the existence of a central focus in the form of a well-known full-time Chairman of BL serves to elevate issues (particularly in the industrial relations field), attract media attention and offset the considerable efforts which have been made to play down the "British Leyland" image and promote the images of the individual product companies and marque names. Thus they agree that the demands on such a leader would continue to be very great. However, they state that the necessary combination of leadership qualities is more easily to be found and deployed in a single Executive Chairman of a unified BL than in two teams, each consisting of a non-executive Chairman and a Chief Executive, as recommended by the Board. They further imply that a successor to Sir Michael Edwardes, possessing all of the necessary qualities and being subject to all the existing pressures on that role, could nevertheless be more successful in lowering the public profile of BL and its Chairman, thus enabling the operating subsidiaries to come through publicly.
3. These conclusions are illogical and contrary to the experience of the BL Board over the last 4 years. Its judgement is that a direct successor to Sir Michael Edwardes would (even if a suitable person could be found) face a much more difficult task than would the leadership of the two new companies under the Board's proposed structure, particularly as he would inevitably be tested (e.g. by left-wing militants) by way of comparison with his predecessor. He could not avoid a high public profile; his status would have to be very considerable at the outset in order to qualify him for the job, and this in itself would attract media attention.

4. Since the consultants envisage that a full separation into two companies would be possible after two more years, a new full-time Chairman would presumably be expected to take on only a 2-year assignment. Given the lengthy learning curve which is inevitable in a company posing such complex and varied problems as BL, this would appear to be a further obstacle to the attraction of a suitable candidate - and it does nothing for continuity.
5. The main grounds on which the consultants appear to question the leadership configuration proposed by the BL Board relate to the balance of responsibility and power between non-executive Chairman and Chief Executive in the two new companies. They suggest that the pressures on a non-executive Chairman would make his position untenable, and that he and the Board might be dominated by the Chief Executive who would tend to be less objective about such issues as major closures or privatisation.
6. The configuration of non-executive Chairman and Chief Executive has been well tried and tested in many major companies. It enables complementary qualities to be brought together at the top of a company which cannot easily be found to co-exist in a single person. Moreover, it is designed specifically to avoid executive dominance of the Board, which is much more likely to occur under an Executive Chairman. Thus the high priority which both Government and Board attach to objectivity would be better fulfilled by putting the chairmanship, together with the majority on the Board, into non-executive hands. In the Board's judgement, the job of non-executive Chairman is manageable in the two new companies, but not in a unified BL. It might require rather more than the traditional 10% of the Chairman's time but not by any means a full-time commitment.
7. The consultants suggest, without any evidence, that the Chief Executives of the two new companies would be inexperienced in taking positions of prominence. On the contrary, senior executives in BL have had considerable experience (by the general standards of British industry) in dealing with both the media and the Government. This has been encouraged by the devolution of responsibility under the present Chairman as BL has evolved towards a two-company managerial structure.

8. The report suggests that a unified structure would best preserve continuity from the present Board and management team, provided that a successor to Sir Michael Edwardes was "supported by the maximum continuity from the present Board". The consultants had no grounds for assuming this would be the case. Indeed it is difficult to understand how they could question the view advanced by the Board, when they were given evidence to the effect that continuity would be more certain under a split structure.
9. The consultants seek to avoid the problems of manageability and continuity in a unified structure by suggesting that Sir Michael Edwardes should continue in the Chairman's role for two further years on a part-time basis. In view of his disagreement with the concept of maintaining a central focal point (a unified BL) he has ruled out this possibility.

OTHER COMMERCIAL AND MANAGERIAL CONSIDERATIONS

10. The report questions the Board's judgement of the balance of advantage between a two-company split and a unified structure in several other commercial and managerial areas.

A. Industrial Relations

The consultants argue that all the Board aim to achieve in the industrial relations field by a two-company structure could equally be achieved by decentralisation of managerial authority and of wage bargaining within a unified structure. The Board's judgement, however, is that the maintenance of a unified BL with a central focal point would detract from the effectiveness of any decentralisation and would continue to attract disproportionate interest from left-wing militants who see BL as a major political target - and that the best way to finesse the militants is to establish two separate entities, fully insulated from one another.

B. Vulnerability

The consultants agree that the balance of the argument on vulnerability favours the Board's proposal but assess this balance as only marginal. They neglect the simplest and most important advantage of a two-company split as against the present centralised financial structure - that, if there is a crisis in one of our major operating companies, only half of the present BL would in future suffer from the uncertainty surrounding that crisis. In present circumstances, this uncertainty (affecting dealer, customer, and collaborator confidence as well as the attitude of BL's bankers) would last for many months because of the triggering of default clauses in BL's loans, resulting in a requirement for

temporary Government guarantees and a lengthy period of financial re-negotiation.

C. Collaboration

The consultants state that other manufacturers wishing to collaborate with a particular part of BL would be as easily attracted by a decentralised management structure within a unified company as by a complete split into two companies. They produce no evidence for this. The Board's belief to the contrary is based primarily on the vulnerability argument above. Potential collaborators with the cars or truck businesses would prefer that their collaborative partners were not subjected to crises of confidence arising from problems in totally separate sectors of the business. Effective insulation of the individual sectors cannot be achieved while a centralised financial and legal structure remains.

D. Central Staff Functions

Paragraph 5.3 of the report, together with paragraph 3 in Exhibit D, comment both on the "undesired loss of central staffs and disturbance to management systems" which the consultants believe could result from the Board's proposal, and on the useful role of central staffs in coordinating policies which have common elements across the various business components.

Quite apart from the conflict of this plainly managerial judgement with the consultants' terms of reference which acknowledged the Board's responsibility in these matters, the consultants have over-estimated both the importance of central staffs in determining the fortunes of the company under the present structure and the risks of disruption due to loss of key staff personnel. If the Government gives early approval to the Board's proposal, sufficient time remains to plan the transfer of staff functions and personnel from BL to the two new companies in an orderly fashion, and with some resulting cost reduction. Below this level, the management of the operating companies is modular and will not be affected by the proposed structure.

The Board's concern, on the other hand, is the very real question of whether we will retain senior line managers under the consultants' proposal.

PRIVATISATION OF LAND ROVER

11. The consultants' case for preserving a unified structure to supervise the total disposal of Land Rover around the end of 1983 rests on two key assumptions:-
 - a. that Land Rover should be sold outright at that stage, bearing in mind possible substantial detriment to related areas of the business;
 - b. that, if the Government wished this to be done, it would be more likely to secure cooperation from the Board of a unified BL than from the Board of the commercial vehicle company under the proposed 2x2 structure.

12. The first of these assumptions should be considered in the context of the following contradictory statements in paragraph 2.5 of the report: "There are substantial interdependencies between the two components, Leyland and Land Rover, both in the UK and overseas. Both businesses, particularly Leyland, are at a fragile stage in their recoveries and changes which do not carry clear bottom line benefits are difficult to justify." Nevertheless, the report goes on to state in the same paragraph, without any evidence, that by end 1983 "the further separation of the Land Rover organisation would be possible without excessive risk to either component and pave the way for early privatisation".

13. The "substantial interdependencies" identified by the consultants are between Land Rover and Leyland Trucks, rather than the Leyland Group as a whole. Leyland Trucks is clearly the most fragile part of the Leyland Group. It is not due, under the 1982 Corporate Plan, to return to profitability until 1984, and a considerable period would be needed to make its overseas operations independent of Land Rover, if this were the agreed course. The synergy between the two is not a temporary phenomenon. Consequently, there is no commercial foundation for the consultants' estimate as to the optimum timing for any total disposal of Land Rover. The timing of total privatisation needs to take account of how Leyland and Land Rover develop and of the total prevailing economic circumstances. Premature privatisation of Land Rover could well require review of the Leyland Trucks Plan.

14. With these factors in mind, the Board has favoured - as an alternative means of attracting private equity capital into Land Rover in the short term - the flotation or sale of a substantial minority stake, if possible by the end of 1983. The report does not consider specifically whether this course would be assisted or otherwise by the 2x2 structure. In BL's view, the split into two companies will be helpful in attracting a minority shareholding into Land Rover because of the complete insulation from BL Cars which would be achieved.
15. As regards the second of the consultants' assumptions, we show in paragraph 6 above that there is no reason to expect a Board with a non-executive majority headed by a non-executive Chairman to be less objective than a Board, albeit with a larger portfolio, headed by an Executive Chairman. Moreover, either form of Board would be guided by commercial considerations and would not regard the premature privatisation of Land Rover as justifiable if it damaged the real prospect of recovery for Leyland Trucks.
16. If, on the other hand, the Leyland Trucks Plan were to fail, then the present Board including the Executive Directors are committed to close Leyland Trucks, and total disposal of Land Rover would then become commercially feasible. Given the continuity envisaged in the 2x2 proposal between the present Board and the Boards and top management of the two new companies, there would be no reason for this commitment - and indeed the commitment of the Board and management to privatisation in an orderly and commercial basis within the recovery strategy - to change.

CONCLUSION

17. The consultants suggest that BL admits there will be no direct bottom line benefit from the 2x2 structure. This is correct, in terms of short-term impact on PBIT, but it overlooks what is perhaps the key issue. This is that the Board considers that the risks to the achievement of the Corporate Plans of BL's various businesses will be substantially reduced if the two-company structure is adopted - and conversely will be seriously increased if there is major discontinuity of top management and a subordination of commercial considerations to the objective of short-term privatisation. Indeed achievability of the Plan could be at risk, so that the bottom line impact of not splitting could be very great.

18. The Board's view, contrary to that of the consultants, is that the 2x2 structure provides greater flexibility to respond to crises and to press ahead with appropriate degrees of privatisation. The Board sees nothing in the report which detracts from the case summarised by the consultants as Exhibit C for moving to a two-company structure in the course of this year.

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DEPARTMENT OF INDUSTRY

ASHDOWN HOUSE

123 VICTORIA STREET

LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301

SWITCHBOARD 01-212 7676

PS/ Secretary of State for Industry

19 March 1982

Michael Scholar Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1

PM has seen

Dear Michael -

BL's FUTURE STRUCTURE

I enclose for the Prime Minister's information a copy of BL's reaction to the Corporate Consultants Group Study on BL's future structure, which should have been enclosed with the Secretary of State for Industry's minute to the Prime Minister of 16 March 1982.

2 Please accept my apologies for any inconvenience caused. I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer, the Secretaries of State for Trade and Employment, and to Sir Robert Armstrong and Mr Ibbs.

*Yours sincerely
Kim Benson*

KIM BENSON
Private Secretary